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CONTROLS ON TRADE WITH COMMUNIST CHINA

Submitted by the

DIRECTOR OF CENTRAL INTELLIGENCE

The following intelligence organizations participated in the preparation of this estimate: The Central Intelligence Agency, and the intelligence organizations of the Departments of State, the Army, the Navy, the Air Force, and The Joint Staff.

Concurred in by the

INTELLIGENCE ADVISORY COMMITTEE

on 11 January 1955. Concurring were the Special Assistant, Intelligence, Department of State; the Assistant Chief of Staff, G-2, Department of the Army; the Director of Naval Intelligence; the Director of Intelligence, USAF; and the Deputy Director for Intelligence, The Joint Staff. See, however, the footnotes taken by various members to specific paragraphs. The Atomic Energy Commission Representative to the IAC and the Assistant to the Director, Federal Bureau of Investigation, abstained, the subject being outside of their jurisdiction.

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CONTROLS ON TRADE WITH COMMUNIST CHINA[1]

THE PROBLEM

To estimate the political, economic, and strategic consequences to China, Sino-Soviet relations, and the non-Communist world of each of the following courses of action:

a. Maintenance of present levels of non-Communist controls on trade with China and the European Bloc;[2]

b. Multilateral relaxation of non-Communist controls on trade with China to the level maintained on trade with the European Bloc;

c. Relaxation of non-Communist controls on trade with China to the level maintained on trade with the European Bloc, but with the US unilaterally maintaining various controls on trade with China.

d. Multilateral raising of non-Communist controls on trade with China.

[1] For general estimates on China and on the Bloc, see NIE 13-54, "Communist China's Power Potential through 1957" (3 June 1954); NIE 10-7-54, "Communist Courses of Action in Asia through 1957" (23 November 1954); and NIE 11-4-54, "Soviet Capabilities and Probable Courses of Action through Mid-1959" (14 September 1954).

[2] As used herein, the term "European Bloc" includes the USSR and the Soviet Satellites in Europe. The term "Bloc" alone is used to cover all iron curtain countries including Communist China. Unless otherwise specified, the terms "China" and "Chinese" are used in lieu of "Communist China" or "Chinese Communists."

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CONCLUSIONS[8]

A. China's objective of creating an industrialized and militarily powerful state cannot be achieved without extensive imports of capital goods and military equipment. The rate of advance of China's power potential thus depends to a large degree on the volume of China's foreign trade. Except to the extent that the USSR extends grants or credits, China's capabilities to import will be limited by its capabilities to export. *(paras 1, 19)*

B. China has been able to import from the European Bloc those commodities, including transshipped Western goods, required for a rapid expansion of military strength and achievement of industrial output somewhat higher than previous peaks. It is committed to a program integrating its economy with that of the Bloc, in consonance with the Bloc policy of autarky. Nevertheless, at present, both Moscow and Peiping give every indication that they regard it in their best interest to increase somewhat their present trade with non-Communist countries and are exerting efforts to undermine trade controls. *(paras 11, 12, 14, 18)*

C. While trade controls have not significantly hindered China in obtaining essential commodities, they have reduced the volume of China's imports by altering its markets and by increasing its transportation costs and procurement difficulties. We estimate that these effects currently represent an annual loss to China of roughly $200 million. This amount would be sufficient to enable China to increase by 50 percent its imports of capital goods, the scarcity of which is particularly serious for the Chinese economy. *(paras 11, 12, 13, 15)*

Effect of Maintenance of Present Levels of Trade Controls

D. Maintenance of present levels of trade controls against China would continue the present effects virtually unchanged although China will be able to take advantage of the recent relaxation of controls enforced against the European Bloc

[8] The Director of Naval Intelligence and the Deputy Director for Intelligence, The Joint Staff, believe that any approach to the problem of relaxation of trade controls should be viewed in the light of over-all Communist objectives, and specifically the attitude and actions of Communist China toward the US and the other Free World nations. They therefore consider it essential to the broad view of the problem that the following be inserted ahead of the present first Conclusion of this estimate:

"There is no indication that the fundamental hostility of the Communists toward the Free World has abated, nor that, in pursuit of their ultimate objectives, the Communist program of attaining self-sufficiency within the Bloc at a high level of military and industrial development has changed. Moscow and Peiping almost certainly estimate that the qualitative and quantitative gains, which would ensue from increased trade with the Free World, will accelerate this planned expansion of their economies, as well as provide opportunities for political gain through economic penetration. We do not believe that any relaxation of controls on trade with Communist China will lessen this hostility, nor will it tend to change the course of Communist China's foreign policy."

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and import additional CHINCOM [4] controlled items via European Bloc countries. While transshipment might add to the total cost of Chinese imports, the additional goods procured would allow the European Bloc greater flexibility in meeting Chinese requirements. *(para 19)*

E. We do not believe that maintenance of trade controls at present levels would produce any significant changes in the basic patterns of Sino-Soviet relationships or of Chinese foreign policy. Chinese propaganda would continue to hold out to other countries the prospect of advantageous trade with China, in order to arouse resentment toward the control system and to encourage policy conflicts with the US. Chinese efforts to achieve political gains in Asia through economic penetration would continue to be hindered by the maintenance of controls. *(paras 20, 21, 22)*

F. If China refrains from provocative military or political actions, pressure would increase in most CHINCOM countries for a reduction of controls to the level applied against the European Bloc. The position of the UK, which plays a major role in influencing the attitude of CHINCOM countries, will continue to be governed more by political than by economic considerations. These countries probably would not override strong US objections to a major change in policy nor would they be likely to take unilateral action to reduce controls. Maintenance of present CHINCOM controls would, however, be a mounting source of irritation in US relations with other CHINCOM countries. *(paras 25, 27)*

Reduction of Controls on Trade with China (CHINCOM Controls) to the Level Maintained with the European Bloc (COCOM [5] Controls)

G. In this situation, almost all the effects of present trade controls in increasing China's import costs and reducing its export receipts would be removed. We estimate that within two years after controls were lowered China might add about $200 million to its annual earnings of foreign exchange, provided its leaders decided to export to the amount necessary to yield these earnings and provided markets were available. However, China would not be able to secure any commodities that it cannot now secure through transshipment. *(paras 28, 32)*

H. China's foreign exchange earnings would almost certainly continue to be used primarily to procure imports of capital goods and other commodities essential to building the modern industrial sector of the economy, and to modernizing the armed forces. We believe that China in the foreseeable future will not be interested in substantial imports of consumer goods. *(para 33)*

I. We do not believe that a relaxation of trade controls would, at least for the next few years, have any significant effect

[4] Fifteen countries currently participate in the China Committee (CHINCOM) of the Consultative Group of countries organized to deal with problems arising from the control of trade with Bloc countries. CHINCOM controls are those controls presently applied by these countries against China. Member countries are: Belgium, Canada, Denmark, France, Greece, Germany, Italy, Japan, Luxembourg, the Netherlands, Norway, Portugal, Turkey, the UK, and the US.

[5] COCOM controls are those applied against the European Bloc (the USSR and the European Satellites) by countries which are members of the Coordinating Committee (COCOM) of the Consultative Group. The membership of COCOM is identical with that of CHINCOM.

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upon China's internal political situation, its foreign policies, or its basic relationship to the USSR.[6] *(paras 34, 35)*

J. A multilateral relaxation of controls on trade with China would probably be approved by most of the governments of Europe and Asia, some because of conviction that it was a desirable move, others out of indifference to the issue or willingness to follow the lead of the powers principally concerned. While Chinese trade with non-Communist countries would probably increase after the relaxation of controls, and in some areas would be exploited for political purposes, it is almost certain that the amount of trade increase would fall far short of expectation in many countries. These countries might, therefore, in the course of time, become somewhat less vulnerable to trade offers made by China for political reasons. Nevertheless, China would probably exert every effort to import such quantities of specialized materials from Western sources as its economy permits. We believe that once these controls were relaxed only open aggression by Peiping would bring about a reimposition of controls. *(paras 36, 37)*

K. We believe it unlikely that trade relations beween China and Japan could regain their prewar significance under any foreseeable circumstances, because of the postwar economic and political changes which have occurred in the Far East. With trade controls at the COCOM level, we believe that by 1957 the value of Chinese exports to Japan might be raised from the present figure of about $40 million a year to about $100 million. The value might even reach $150 million, but we believe this would require some diversion of Chinese exports from Bloc markets. We believe that Sino-Japanese trade during the next few years will not in itself cause Japan to alter significantly its present orientation to the West barring a serious depression in the Free World accompanied by a drastic curtailment of Japanese trade opportunities.[7] *(para 39)*

Effects of a Reduction of CHINCOM Controls to the COCOM Level, but with the US Unilaterally Maintaining Various Alternative Levels of Controls

L. In this situation we believe that: (a) if the US maintained its present complete embargo on both imports and exports, the foreign exchange advantages which the Chinese might otherwise gain would be reduced by roughly one-half; (b) if the US maintained only a ban on imports from and remittances to China, the potential gains in foreign exchange to China would be reduced by about the same proportion; and (c) if the US maintained

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[6] The Deputy Director for Intelligence, The Joint Staff, would add the following sentence (taken from para. 34): "However, increased trade with the West would reduce certain strains which probably exist in the Sino-Soviet relationship."

[7] The Deputy Director for Intelligence, The Joint Staff, believes this sentence should be replaced with the following:
"Nevertheless, China's need for capital goods and its available or foreseeably available raw materials complement the present economic situation of Japan — productive capacity excess to its own needs, a diminished raw materials base, and an unfavorable balance of trade without substantial exports. It would be very much to Communist advantage if Japanese heavy industry were to supply much of the means for China's industrialization, particularly if at the same time Japan were to become partially dependent on China as a raw materials source and capital goods market. Current trade overtures indicate Communist awareness of this opportunity, and Japanese willingness to participate in such a pattern of trade."

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only a ban on exports to China, the Chinese could procure equivalent commodities elsewhere at only slightly increased costs, and could spend in other countries the dollars earned by exports to the US. *(paras 40, 41, 42)*

M. Although trading interests in CHINCOM and Far Eastern countries would welcome the continued absence of US competition in the Chinese market, their governments would be concerned at the divergence of their policies from those of the US. There would probably be apprehension that the failure of the US to participate in the general relaxation of controls would contribute to a continuation of tensions in the Far East. Moreover, difficulties and frictions would probably arise if the US attempted to prevent the re-export to China from third countries of goods imported from the US. *(para 44)*

Effects of Raising the Present Level of CHINCOM Controls

N. A further increase in controls on exports to China — without a corresponding increase in the level of COCOM controls — would probably have the effect of increasing the volume of transshipped goods, but it would probably not appreciably retard China's internal development. If an embargo on imports from China, similar to that now applied by the US, were applied by all CHINCOM countries, China would lose export markets now taking about one-quarter of total exports (including Bloc re-exports of Chinese products). Since Bloc markets are not believed to be readily expansible, it is probable that China's import capabilities would be reduced proportionately. Such a reduction in China's imports would significantly retard China's internal development. *(paras 45, 46)*

O. The Director of Central Intelligence, and the Special Assistant, Intelligence, Department of State, believe that in the unlikely event that *all* non-Bloc shipping and shipping services were denied to the uses of Chinese commerce, the Chinese economy would in the short term be adversely affected, and transportation costs increased. Non-Bloc ocean-going vessels in 1953 carried about three-fourths of China's seaborne foreign trade. Bloc flag shipping is inadequate to carry its own trade and no substantial building program is in progress. However, a substantial share of China's seaborne trade now carried in non-Bloc vessels would be carried by the Trans-Siberian railroad and by Bloc flag vessels diverted to the China trade, provided non-Bloc flag vessels were chartered to replace the shipping so diverted. A considerable part of the trade probably would be curtailed, notably China's exports of coal and iron ore which constitute 40 percent of seaborne export tonnage but less than 1 percent of the value of total exports. These adjustments would probably be made within a reasonable period. If denial affected only CHINCOM flag shipping and services, the Chinese could shift at least part of their seaborne commerce to non-CHINCOM flag vessels, thus mitigating still further the effects described above. *(para 48)*

P. The Director of Naval Intelligence; the Deputy Director for Intelligence, The Joint Staff; the Assistant Chief of Staff, G–2; and the Director of Intelligence, USAF, believe that in the unlikely event that *all* non-Bloc shipping and shipping services were denied to the uses of Chinese

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commerce, the effects upon the Chinese economy would be marked and adverse. It is probable that only a small portion of the tonnage now carried by non-Bloc ships could be carried through an increase or readjustment in the use of Bloc shipping. Denial of all non-Bloc shipping would result in considerable curtailment of China's foreign trade, because the rail transportation facilities within China and those between China and the European Bloc probably are not adequate to handle the additional tonnages involved. If denial affected only CHINCOM flag shipping and services, the Chinese could shift at least part of their seaborne commerce to non-CHINCOM vessels, thus mitigating the effects described above. We believe, however, that the extent of this mitigation would not be significant, since the denial of shipping services (reinsurance, bunkering, repair, etc.) by the largest maritime nations, in addition to other pressures which could be brought to bear, would make most non-CHINCOM countries extremely reluctant to commit their vessels to this trade, despite the probability of premium charter rates being offered by the Bloc. Few non-CHINCOM countries have substantial additional tonnage suitable for the China trade, and with few exceptions, the availability of any vessels would be limited by the extent to which they could be replaced on their regular runs by shipping chartered from CHINCOM countries. Moreover, of all non-CHINCOM countries, only Sweden has a significant amount of shipping which could be so used. *(para 49)*

Q. Without some new and considerable provocation by China or possibly the USSR, we believe that an appreciable increase in the level of controls on trade and shipping with China would almost certainly not be agreed to by non-Communist countries. *(para 50)*

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INTRODUCTORY NOTE ON THE PRESENT SYSTEM OF CONTROLS

Although single countries, particularly the US, had applied trade controls against the European Bloc earlier, international agreement for such controls came into effect with the establishment by the major Western allies of the Coordinating Committee (COCOM) in January 1950. The member states [8] agreed to three lists of commodities, based on the relative importance of the items listed as a contribution to the military potential of the Bloc. Goods on International List I (IL–I) are completely embargoed; goods on IL–II are subject to certain quantitative controls; and goods on IL–III are subject to surveillance and exchange of information between the COCOM countries.

In June 1950 China and North Korea were brought within the scope of the export controls exercised by the COCOM countries. In December 1950, after the Chinese aggression in Korea, the US applied a complete embargo to China. Following the UN embargo resolution of 18 May 1951, the COCOM countries tightened their controls, and 30 other countries imposed restrictions on their exports to China. By the fall of 1952, when a China Committee (CHINCOM) [9] was formed by the COCOM members to control trade with China, all COCOM countries had agreed to embargo all three COCOM categories as well as certain supplementary items proposed by the UK (China Special List). Some countries have unilaterally embargoed additional strategic items, but among the major trading nations only the US has a complete embargo on all trade with China. In addition, certain transshipment controls are currently applied by the US and UK, and are being adopted by certain other COCOM countries. The US and Greece have an embargo on imports from China and North Korea; the US, Canada, and the Netherlands have adopted controls on financial transactions, and certain other COCOM countries including the UK are adopting such controls. Practically all leading non-Communist maritime countries prohibit their merchant ships from carrying strategic goods in the China trade, and the US, UK, France, and Japan have adopted bunkering controls. However, these measures have been too limited in scope to prevent the Bloc from obtaining the use of a substantial volume of Western shipping for China's overseas and coastal trade. All CHINCOM controls have been subject to frequent circumvention and some violation.

As the result of continued pressure by most non-Communist countries, major adjustments, chiefly relaxations, were made in August 1954 in the COCOM system of controls over trade with the USSR and its European Satellites (but not in the CHINCOM system of controls over trade with China). These adjustments were generally in keeping with the objectives, set by the Paris Consultative

[8] Fifteen countries currently participate in COCOM: Belgium, Canada, Denmark, France, Greece, Germany, Italy, Japan, Luxembourg, the Netherlands, Norway, Portugal, Turkey, the UK, and the US.

[9] Same 15 countries participating in COCOM.

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Group,[10] of establishing the control lists on a "long haul" basis and giving appropriate recognition to particular economic and political pressures within individual countries. The relaxation in controls against the European Bloc took the form of net reductions in the number of items or categories in the embargo, quota, and surveillance control lists by 37 percent, 77 percent, and 40 percent respectively, and, even more important, a redefinition and downgrading of many items from the embargo list to the quota and surveillance lists. These adjustments have widened the differential between controls on trade with the European Bloc and controls on trade with China, and therefore increased the opportunities for China to get through other Bloc countries items it could not get direct. However, in relaxing controls against the Bloc, the COCOM countries agreed to consider measures that would prevent or reduce such indirect trade. A Transit Authorization Certificate (TAC) system has been agreed upon whereby unrestricted use of the free ports in COCOM countries for evasion by transshipment would be precluded for items on IL–I.

DISCUSSION

EFFECT OF PRESENT CONTROLS ON CHINA

China's Foreign Trade

1. Foreign trade is essential to China so long as its leaders have as an objective the creation of an industrialized and militarily powerful state. The heavy industry of China cannot for a number of years produce more than a relatively small fraction of China's total requirements for capital goods and military equipment. These therefore must be imported. The rate at which China's economy and military forces are developed and strengthened will therefore be determined largely by China's ability to obtain imports essential to its programs in return for the agricultural products and mineral raw materials which it can export.

2. Since 1950 China has succeeded in increasing its foreign trade and has concentrated on importing military equipment, capital goods, and industrial raw material. China's trade has also been markedly redirected toward the Bloc and away from non-Communist countries.

ESTIMATED VALUE OF CHINA'S TOTAL FOREIGN TRADE, 1950–1954
(US $ millions)

Year	Total Value	Soviet Bloc		Non-Bloc Countries	
1950	$1,082	$282	26%	$800	74%
1951	2,164	1,319	61%	845	39%
1952	1,780	1,280	72%	500	28%
1953	2,200	1,615	73%	585	27%
1954 (Prelim)	2,200	1,650	75%	550	25%

3. The delivery of Soviet military equipment and supplies accounted in large part for the sharp rise in China's trade with the Bloc between 1950 and 1951. Through 1953, these deliveries probably accounted for nearly one-half of China's imports from the European Bloc. Not included in the trade figures are the substantial quantities of military equip-

[10] The Consultative Group (CG) is composed of representatives of countries participating in the COCOM trade control system. Its permanent working committee is the Coordinating Committee (COCOM). The main functions of CG are to review the recommendations of COCOM, to consider general policy matters arising in COCOM, and to set the general frame of reference for future COCOM activities.

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ment which we believe the USSR gave to China on a grant basis. Capital goods probably accounted for one-third of Chinese imports from the European Bloc and included equipment for the metallurgical, chemical, and machine tools industries, power generating equipment, machinery, trucks, steel products, and metals. The remaining imports consisted of raw materials, such as petroleum and chemical products, and essential consumer goods.

4. Except for the military equipment received on a grant basis and Soviet credits of at least $430 million ($300 million for the period 1950–1954 and $130 million for the period 1955–1959) China has apparently financed its imports from the European Bloc with its own exports: substantial quantities of agricultural products (including soy beans, vegetable oils, and grains), mineral raw materials (including tin, antimony, coal, iron ore, and wolfram), and pig iron. Some of these exports have been diverted or resold to Western nations, in part for the European Bloc account.

5. China's trade with non-Communist countries since 1950 has been substantially in balance except in 1951 when foreign exchange balances were liquidated. China has paid for its imports (raw cotton, crude rubber, fertilizers and other chemicals, iron and steel, and machinery) largely by exporting foodstuffs, vegetable oils, and coal. There is evidence of a deterioration in China's terms of trade with non-Communist countries since 1950. A portion of this deterioration apparently stems from the fact that political rather than economic considerations have influenced China's trade with certain non-Communist Asian countries. Commodity composition of China's recorded [11] imports from non-Communist countries since 1950 is estimated roughly as follows:

CHINESE *RECORDED* IMPORTS FROM NON-COMMUNIST COUNTRIES, 1950–1954

(US $ millions)

Year	Cotton	Rubber	Drugs	Other Chemicals	Metals Machinery Equipment	Other	Total
1950	$95	$61	$20	$35	$125	$78	$414
1951	41	110	25	65	110	93	444
1952	108	23	25	40	20	34	250
1953	16	54	40	55	70	45	280
1st half 1953	4	28	30	30	40	32	164
2nd half 1953	12	26	10	25	30	13	116
1st half 1954	35	17	20	25	10	30	137

6. The principal sources of China's *recorded* imports from non-Communist countries have changed since 1952 in the direction of increased trade with Western Europe. The 1953 four-fold increase over 1952 in direct Western European exports to China resulted largely from the fact that Western Germany, the UK, France, and Switzerland increased their exports to China of iron and steel, machinery and instruments, chemicals, and wool. However, as a result of the imposition of controls on the export of iron and steel to China (effective August 1953), Western European exports declined in the second half of 1953 and remained at a lower level in 1954. Pakistan

[11] Recorded trade is that identified and reported by the country of origin or shipment as destined for China. China acquires additional imports by transshipment and smuggling activities (see paragraph 7).

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raw cotton exports to China declined from $95 million in 1952 to $4 million in 1953; but increased again in 1954. Imports from Japan have increased rapidly following the reduction of Japanese export controls to the CHINCOM level.

CHINA'S *RECORDED* IMPORTS FROM NON-COMMUNIST COUNTRIES BY EXPORTING AREAS

(US $ millions)

Exporting Area	1952	1953	1954 [1]
Western Europe	$23	$100	$71
Hong Kong	86	95	64
Japan	1–	5	15
Pakistan	95	4	36
Ceylon	23	55	48
All Other Areas	22	21	34
Total	$250	$280	$268

[1] Annual rate based on nine months.

7. In addition to these recorded imports, which were for the most part shipped direct to China from the areas of origin, China obtained substantial unrecorded imports from non-Communist countries. In 1953, such imports were estimated to be $93 million or about one-third of total recorded imports from non-Communist countries. Of this total, $65 million (including about $50 million in iron and steel) was accounted for by goods diverted to China after leaving Western European countries of origin ostensibly for destinations other than China. Most of these diverted goods were transshipped to China-bound vessels at Gdynia. In addition, an estimated $12 million unrecorded imports entered China through Macao, an estimated $8 million in strategic commodities (including copper, zinc, aluminum, spare parts, transmitting tubes, and other electronic materials) were smuggled in via Hong Kong, and an estimated $8 million unrecorded imports were received from all other areas.

8. In summary, imports (including both recorded and unrecorded) from non-Communist countries declined from 79 percent of total imports in 1950 to 34 percent in 1953. This primarily reflects a great increase in imports from the European Bloc. At the same time, total imports from non-Communist countries, including recorded, unrecorded, and smuggled trade, amounted to approximately $373 million, or about 90 percent of the value of such imports in 1950. Within the total of these imports there has been an increase in the proportion of goods important to the expansion of the Chinese economy, such as chemicals, metals, machinery and equipment.

9. We estimate that roughly one-half of the volume of China's trade was carried by sea. The other half was carried overland, largely over the Trans-Siberian railway.[12] To carry its overseas trade, China relies on the shipping of other flags, largely non-Bloc, for China itself possesses practically no ocean-going shipping [13] and that available from other Bloc countries is inadequate. Thus in 1953, 85 percent of the ships calling at Chinese ports were of non-Communist flag. Of these, 60 percent were of British registry. Most of the ocean-going coastal trade of China in the area between Hong Kong and Shanghai has been carried by non-Communist shipping; under conditions imposed by the Nationalist blockade, practically all is so carried. North of Shanghai, where the bulk of the Bloc shipping is concentrated, non-Communist vessels carry part of the trade.

10. Both Moscow and Peiping apparently desire some increase in East-West trade, and believe that such an increase would contribute to Bloc interests. However, if any such increase took place, it would be carefully limited by Communist leaders to trade in those commodities and through those channels which would serve their foreign political and economic objectives, and would hasten the expansion of their respective economies. It would not be allowed to endanger the program of Bloc autarky or to risk the development of any appreciable economic dependence of the Bloc on the non-Communist world.

[12] See footnote to the table on page 11 taken by the Director of Naval Intelligence and the Deputy Director for Intelligence, The Joint Staff.

[13] Ocean-going shipping includes only vessels 1,000 gross registered tons or over.

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ESTIMATED GEOGRAPHIC DISTRIBUTION OF CHINA'S FOREIGN TRADE, 1953**

Country	Value (US $ millions) Imports	Value (US $ millions) Exports	Volume (thousands metric tons) Imports	Volume (thousands metric tons) Exports	Principal Means of Transport
Non-Bloc					
Hong Kong and Macao	$115	$153	260	750	Coastal, small vessels, rail
Ceylon	55	40	70	300	Ocean vessels
Western Europe *	100	130	420	1,000	Ocean vessels
Other non-Bloc	38		60		
Unrecorded imports transshipped from Western Europe	65	....	235	.....	Ocean vessels
Subtotal	373	323	1,045	2,050	–
Bloc					
Seaborne:					
European Bloc	100	80	370	985	Ocean vessels
Soviet Far East	12	27	160	250	Ocean vessels
Overland:	615	670	1,500–2,000	2,500–3,500	Rail
Subtotal	727	777	2,030–2,530	3,735–4,735	
Grand total	$1,100	$1,100	3,075–3,575	5,785–6,785	

* Including transshipments via Eastern European ports of recorded imports from Western countries amounting to an estimated 80,000 tons valued at US $20 million.

** The Director of Naval Intelligence and the Deputy Director for Intelligence, The Joint Staff, believe that the actual percentage of China's foreign trade carried by sea is considerably larger than expressed in this Table, from which the corresponding estimate in paragraph 9 was derived. This belief is based upon the following considerations:

a. Estimates of the capacity of the inland transportation systems serving Communist China are predicated to a large extent upon incomplete and insufficiently corroborated evidence. For this reason, these estimates should be regarded with reserve as being subject to a possible large margin of error.

b. On the other hand, the minimum amount of seaborne tonnage entering and leaving Communist China is known from reliable information, including ship movements, visual observations, and masters' reports. This seaborne tonnage derived as above represents a minimum. It excludes 139 arrivals in 1953 alone representing about 620,000 gross registered tons of shipping on which no cargo information is available. It is believed therefore, that the figures are considerably larger, but the extent of the increase cannot be determined due to inability to ascertain cargo tonnage actually carried.

c. The known cargo figures actually represent only about 15% of the cargo capacity of the non-Bloc shipping engaged in trade with China.

Therefore, in arriving at an estimate of the respective tonnages carried by sea and land transport, this paper deals on the one hand with estimated rail capacity figures of questionable reliability and on the other hand with firm minimum figures of known seaborne tonnage. It does not attempt to compare estimated rail capacity with known shipping capacity, or to consider the fact that the apparently low percentage utilization of this chartered capacity would be extremely costly and inefficient.

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Effects of Controls on China's Power Potential

11. The effect of trade controls on China is difficult to calculate exactly, for Bloc policies of autarky, the repercussions of the Korean War, and the Chinese program for industrialization have also influenced the military and economic development of China during this period. Nevertheless, we estimate that trade controls have (a) limited the availability to China of certain commodities which would assist military and industrial development, and (b) have reduced the total volume of China's imports through altering China's markets and increasing transport costs and procurement difficulties.

12. The first factor has been of limited importance in retarding the development of China's power potential since China has received from the European Bloc sufficient controlled commodities to make possible a rapid expansion of military strength and achievement of industrial output somewhat higher than previous peaks. It has also obtained some controlled commodities through transshipment and smuggling. However, the difficulties of obtaining replacement parts for Western equipment and some specialized commodities in short supply in the European Bloc probably has created problems, particularly in the fields of transport, communications, and electric power.

13. The second factor — the effect of trade controls in reducing China's total import capabilities — has been of greater importance. The magnitude of the effect may be illustrated if it be assumed that controls had been abolished during 1953, and that various adjustments (which would in fact take a considerable time) had been immediately made. In such a case we estimate that China might during that year have increased its total volume of imports by 20 percent or roughly $200 million since it would have been free from the effects of: (a) the exclusion of its exports from the US market; (b) the US controls on remittances to China; (c) China's restriction of its exports to Japan as a result of Japan's unwillingness to supply strategic commodities in return; (d) the premium prices paid to Western suppliers for controlled or "borderline" goods; and (e) the additional transport costs involved in transshipment or smuggling, or in the transport of bulky materials — such as POL and grains — via the Trans-Siberian railroad. These losses represent a reduction in the resources available to the government.

14. Trade controls, aside from munitions controls, have rendered the task of building up the strength of the Chinese armed forces somewhat more difficult than it might otherwise have been. However, owing to the priority assigned to the military program, the Chinese military build-up was largely insulated from the adverse effects of trade controls. The USSR has provided China with tanks, trucks, artillery, aircraft, ammunition, modern engineering equipment, and petroleum. China has produced infantry weapons, ammunition, crude engineer supplies, clothing, and food for its armed forces. The availability of military supplies from foreign and domestic sources has been sufficient to produce a formidable increase in the combat potential of the Chinese forces. This increase in combat potential is not backed by an adequate industrial base, nor by adequate reserve munition stocks. To the extent that trade controls have slowed China's industrial expansion they have retarded the growth of its military potential.

15. The burden imposed by trade controls on China falls primarily on the Chinese economic program. Through the imposition of stringent internal controls, the regime has been able to mobilize a large volume of resources for investment, and, largely through the rehabilitation and maximum operation of existing facilities, has been able to expand industrial output at a rapid rate. However, the estimated losses attributable to trade controls in 1953 were equivalent to at least five percent of China's total investment. To a considerable degree, moreover, activation of China's investment resources requires the importation of machinery, equipment, and other goods not produced in China's rudimentary industrial economy. Limited capital goods imports are believed to have been a serious problem in

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China's investment program and have been cited several times by the regime as a major cause for failing to meet certain investment goals. Thus, if the entire $200 million in resources estimated to have been lost in 1953 as a result of trade controls had been available for capital goods imports, it would have represented an increase of about 50 percent in such imports and would have enabled the regime to utilize its total investment resources with greater effectiveness.

Effects on Sino-Soviet Relations

16. Non-Communist trade controls have reinforced the deliberate policies of China and the USSR, manifested since 1949, to seek closer political and economic accommodation. The trade of China had begun to be directed towards the Soviet Bloc and away from non-Communist countries even before the imposition of trade controls. This redirection was accelerated and the scope of Chinese trade with the Bloc increased by non-Communist trade controls, but over a period of time these developments would almost certainly have occurred to a considerable degree because of the general drive in the Bloc to reduce dependence on trade with non-Communist countries.

17. The increased level of trade between China and the Bloc probably has required considerable economic adjustments in both China and the European Bloc, although there is scope for mutually advantageous trade between the two areas. Such evidence as there is suggests that China's terms of trade with the European Bloc have not been generally disadvantageous, indicating that the economic adjustments involved in this trade have probably been made by both sides. However, to some extent the commodities and products that China needs to expand its economy are the same as those required to expand the economies of the USSR and its Satellites. In the process of close economic collaboration, China probably has pressed for greater economic assistance than the USSR has been willing to provide.

18. It is probable therefore that non-Communist trade controls have caused some stresses and strains within the Bloc. These strains are probably reflected in the present interest of both Peiping and Moscow in increasing China's trade with non-Communist countries. However, such strains are probably only a minor factor working for or against perpetuation of the Sino-Soviet alliance.

PROBABLE EFFECTS OF MAINTENANCE OF PRESENT LEVELS OF TRADE CONTROLS AGAINST CHINA

Effects on China's Economic and Military Development

19. The maintenance of present levels of non-Communist trade controls would result in little further change in the present pattern and direction of China's foreign trade. The direct effects of non-Communist trade controls — the expenses of transshipments, premium prices for certain goods, denial of foreign markets, and restrictions on remittances from abroad — would continue to operate adversely on China's import capabilities. The recent widening of the differential between controls against the European Bloc and controls against China provides the European Bloc with greater flexibility in meeting China's needs, particularly those items in short supply within the Bloc. In the long run, however, China's total capability to import will continue to be limited by its ability to export.

Effects on Sino-Soviet Relations

20. Since the Sino-Soviet alliance continues to be governed by more fundamental considerations than the amount of trade between China and the non-Communist world, it is unlikely that continuance of controls would produce any additional strains or difficulties in this alliance.

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Effects on China's Foreign Policy

21. China, while developing its subversive capabilities in neighboring countries, is seeking both international acceptance as a world power and leadership in Asia. Recognizing the US as the chief obstacle to the achievement of its objectives, it seeks to isolate the US on Asian issues by contrasting US "intransigeance" with its own "peaceable and reasonable" attitude.

22. The Chinese consider trade controls an affront to their international prestige. Chinese efforts to achieve political gain through economic penetration of other Asian countries, and especially of Japan, will be hindered by maintenance of non-Communist controls on trade. At the same time they recognize that these controls provide them with an especially useful issue in their effort to isolate the US from its allies. They will continue to hold out to other countries the prospect of advantageous trade with China in order to arouse resentment toward the control system and policy conflicts with the US. [14]

Effects on Non-Communist Countries

23. The attitudes of most non-Communist countries toward controls on trade with China are presently more a reflection of their respective views on China policy in general than of any vital necessities arising from their trade situation. Trade with China does not now constitute a significant portion of the foreign trade of any area other than Ceylon and Hong Kong.

24. Since the Korean armistice, and particularly since the recent relaxation of trade controls against the European Bloc, political and commerical pressures have mounted within various CHINCOM countries for a similar relaxation of trade controls against China. In part these pressures are based on the belief that any increase in peaceful intercourse between China and the Free World would tend to reduce both the danger of armed conflict and the dependence of China on the USSR; and that with the end of hostilities in Korea and Indochina, China should be treated in the same manner as the rest of the Bloc. In part they are based on the belief that with the reduction of COCOM controls, CHINCOM controls can readily be circumvented by transshipments through the European Bloc, with the consequence that their principal adverse effect is felt, not by China, but by non-Communist interests related to direct trade with mainland China, notably in Hong Kong and Japan. In addition certain business and labor groups favor a relaxation of trade controls primarily in the interest of increased trade. Other groups are not impressed by the above arguments and believe that a relaxation of trade controls would not in fact result in any appreciable increase in trade and would advance the cause of Communism. On balance, we believe that many governments, particularly among CHINCOM countries, tend to favor some relaxation in controls on trade with China. However, we believe that none of these governments favors abolition of controls.

25. Among the CHINCOM countries other than the US, the position of the UK is of major importance in influencing the attitude of the group as a whole. Interested business groups and political elements in both the conservative and labor parties have placed the British Government under increasing pressure to sponsor or support a relaxation of controls against China. Political rather than economic considerations probably will continue to govern British policy in dealing with this question, which is viewed as subordinate to the complex of issues affecting British relations with both the US and China.

26. In Asia the issue of trade controls against China is of importance to Ceylon, Burma, Indonesia, and Japan, in addition to Hong Kong and Macao. Especially in Japan, there has been considerable agitation for increased

[14] The Deputy Director for Intelligence, The Joint Staff, also believes that Communist freedom of action will continue to be limited to a degree by the threat of imposition of more stringent multilateral controls, so long as the control system as a framework for collective action exists.

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trade with China in the expectation that such trade would help solve a variety of national economic problems (some of which stem from loss of control of North China, Manchuria, and Korea) and would contribute to the relaxation of international tensions. In these countries opposition to the trade control system would become even stronger if free-world markets for their commodities became less favorable. Ceylon, which exports large amounts of rubber to China, is a member of neither CHINCOM nor the UN.

27. If China refrains from provocative military or political actions, pressure would increase in most CHINCOM countries for a reduction of controls to the level applied against the European Bloc. These countries probably would not override strong US objections to a major change in policy nor would they be likely to take unilateral action to reduce controls. Maintenance of present CHINCOM controls would, however, be a mounting source of irritation in US relations with other CHINCOM countries.

PROBABLE EFFECTS OF MULTILATERAL RELAXATION OF TRADE CONTROLS AGAINST CHINA TO THE LEVEL APPLIED AGAINST THE EUROPEAN BLOC [15] [16]

Effects on China's Economic and Military Development

28. If present trade controls applied against China by non-Communist countries were reduced to the level applied against the European Bloc, China would not be able to secure any additional commodities that it cannot now secure through transshipment. Almost all of the effects of present trade controls in increasing China's import costs and reducing its export receipts would be removed. It would greatly facilitate the movement of seaborne cargo to China by enabling the Communists to use normal Western shipping channels rather than transloading and reshipping via Bloc or chartered bottoms.

29. The US formerly provided an almost unique market for many of China's important exports, such as tung oil, bristles, feathers, and handicrafts. Some of these items represent by-products and the resources required for their production is not great. Reduction of US controls from complete embargo to COCOM levels would enable China to: (a) secure a net increase in its total export volume through exporting to the US commodities that it cannot export elsewhere, and (b) secure better prices for other export products owing to the increase in world market demand. China would probably have difficulty regaining its markets in the US and in any case this process would require time. We estimate that within two years China could increase its net export earnings by $60 to $80 million if it had free access to the US market.

30. US financial controls have also deprived China of overseas remittances, which before the imposition of restrictions provided China with a substantial amount of foreign ex-

[15] Since there are no quotas presently applicable to China trade, it is assumed that if controls on trade with China were reduced to levels applying to the European Bloc, appropriate quotas under International List II would be agreed to by CHINCOM. It is also assumed that under any relaxation of controls, enforcement would be at least as effective as that which has thus far been achieved for present controls.

[16] The argument in the following paragraphs is based on the assumption that CHINCOM controls are reduced to the *present* COCOM levels. It might be possible, however, to add selected items to the present COCOM lists primarily to prevent their transshipment to China. We do not attempt in the present estimate to determine which particular goods might most usefully be put on the COCOM lists for this purpose, or whether it would be feasible to negotiate such an enlargement of the lists with the other countries concerned. It seems clear that the effects of such a course of action on China would lie somewere between those described in the preceding section and those described in this section.

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change. We estimate that if the prohibition on such remittances were removed China might acquire as much as $30 to $50 million annually in foreign exchange.

31. With respect to Japan,[17] the other nation principally to be affected by a relaxation of trade controls against China, we believe that the value of Chinese exports to Japan might be raised by 1957 from the present figure of about $40 million a year to about $100 million. The value of these exports might even reach $150 million, but we believe this would require some diversion of Chinese exports from Bloc markets.[18]

32. The estimated additional increments of foreign exchange which China might acquire after a relaxation of present trade controls to the COCOM level are summarized in the following table:

ESTIMATED POTENTIAL INCREASE OF CHINA'S ANNUAL FOREIGN EXCHANGE EARNINGS* AS A RESULT OF MULTILATERAL RELAXATION OF TRADE CONTROLS AGAINST CHINA TO THE LEVEL APPLIED AGAINST THE EUROPEAN BLOC

(US $ MILLIONS)

Source	Increased Receipts of Foreign Exchange	Reduced Costs in Foreign Exchange	Total
US Markets * *	$60 – 80	. . . .	$60 – 80
Overseas Remittances	30 – 50	. . . .	30 – 50
Reduced Transport Costs	. . . . .	15 – 20	15 – 20
Price Differentials	. . . . .	25 – 30	25 – 30
Japanese Trade * *	35 – 50	. . . .	35 – 50
	$125 – 180	$40 – 50	$165 – 230

* Does not include consideration of about $100 million of Chinese assets blocked in US.

** Total increases in earnings would be in excess of these amounts but not all of the increase could be attributed to relaxation of trade controls.

Assuming that the Chinese decided to export to the extent necessary to yield the foreign exchange in the above table, we estimate that within about two years they could increase their imports by about 20 percent over the 1954 estimated level. The value of the additional goods imported would be equal to about 10 percent of the total amount currently allocated to industrial and transportation investment in the Chinese budget. It is important to note that this available foreign exchange, together with additional sources of supply for goods, would permit a considerably more flexible and efficient employment of total investment resources.

33. We do not believe that China in the foreseeable future will be interested in substantial imports of consumer goods from Japan or from any other country. This estimate rests largely on our belief that China will continue to place overriding emphasis on imports of commodities essential to building its modern industrial sector, particularly heavy industry and transportation, and in modernizing its armed forces.

Effects on Sino-Soviet Relations

34. Multilateral relaxation of controls against China would not significantly affect Peiping's relations with Moscow. However, increased trade with the West would reduce certain strains which probably exist in the Sino-Soviet relationship. Although there appears to be no likelihood of China's dissociating itself from the USSR, broader and more regular contact by China with the non-Communist world and greater ease in procuring needed imports might in the very long run permit Peiping to move toward a position of greater independence within the Bloc.

[17] See the Appendix for a brief analysis of the prospects for Japanese trade with China.

[18] The Deputy Director for Intelligence, The Joint Staff, would add: "The Soviet delegate to the UN trade conference at Hong Kong estimates Japan could earn another $300 million in 1956 if trade embargoes were lifted, which highlights the consequences of even a partial reintegration of the economies of Japan and of China. China is committed to a sustained effort to build an industrial economy. Trade with Japan is to its advantage only so long as it contributes to the growth of this economy or can assist in achieving Communist political goals. If and when Japan becomes markedly dependent on the Asian Communist Bloc as a source of raw materials and as a market for its heavy industry, it will be vulnerable to Communist economic pressures.

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Effects on China's Foreign Policy

35. Multilateral relaxation of controls on trade with China would not lead to any alteration in Communist objectives in Asia, nor probably to any substantial changes in China's foreign policy. One of Peiping's propaganda weapons against the US would be lost, but others would remain, and the relaxation of controls would probably be exploited as a considerable victory. Given the totalitarian nature of the Chinese regime, its leadership would find no difficulty in limiting any "liberalizing" effects on Chinese public opinion which might arise from increased trade and contacts with the West.

Effects on Non-Communist Countries

36. A multilateral relaxation of controls on trade with China would probably be approved by most of the governments of Europe and Asia, some because of conviction that it was a desirable move, others out of indifference to the issue or willingness to follow the lead of powers principally concerned. The policy would probably arouse major criticism only in Taiwan and South Korea, both of whose governments would almost certainly continue to observe their present restrictions. In the rest of Asia, US relaxation of trade controls against China would probably be viewed with some disquiet, despite the official approval given the policy by governments. It would probably arouse apprehension among some anti-Communist groups that the US might fail to give active resistance to the further expansion of Communism in Asia. The intensity of such feelings would depend largely on the manner in which the US adopted such a relaxation of controls and on other indications of US policy which were available at the same time.

37. While Chinese trade with non-Communist countries would probably increase after the relaxation of controls, and in some areas would be exploited for political purpose, it is almost certain that the amount of trade increase would fall far short of expectation in many countries. It would not prove to be the panacea for economic ills that some of their peoples have hoped for. These countries might, therefore, in the course of time, become somewhat less vulnerable to trade offers made by China for political reasons.

38. We believe that once these controls were relaxed, only open aggression by Peiping would bring about a reimposition of controls.

39. We believe it unlikely that trade relations between China and Japan can regain their prewar significance under any forseeable circumstance.[19] There has been a fundamental change in the Chinese economic situation since the establishment of the Communist regime. China is now firmly committed to a program of industrialization and of integrating its economy with that of the Bloc. As for Japan, it no longer possesses the political control over Manchuria which permitted it to develop that area as an integral part of its own economy and to make China by far its most important trading partner. Japanese prospects for maintaining an expanding economy will depend far more on its trade with the non-Communist world than on any foreseeable growth in its trade with China. We believe that Sino-Japanese trade during the next few years will not in itself cause Japan to alter significantly its present orientation to the West barring a serious depression in the Free World accompanied by a drastic curtailment of Japanese trade opportunities.[20]

[19] See the Appendix for a brief analysis of the prospects for Japanese trade with China.

[20] The Deputy Director for Intelligence, The Joint Staff, would replace the last two sentences with the following:

"Nevertheless, China's need for capital goods and its available or foreseeably available raw materials complement the present economic situation of Japan — productive capacity excess to its own needs, a diminished raw materials base, and an unfavorable balance of trade without substantial exports. It would be very much to Communist advantage if Japanese heavy industry were to supply much of the means for China's industrialization, particularly if at the same time Japan were to become partially dependent on China as a raw materials source and capital goods market. Current trade overtures indicate Communist awareness of this opportunity, and Japanese willingness to participate in such a pattern of trade."

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PROBABLE EFFECTS OF THE US UNILATERALLY MAINTAINING VARIOUS ALTERNATIVE LEVELS OF CONTROLS ON TRADE WITH CHINA

Effects on China's Economic and Military Development

40. If the US unilaterally maintained present controls [21] against China while other non-Communist countries relaxed controls to the level now applied against the European Bloc, the advantages which the Chinese would otherwise gain from a general relaxation of present trade controls would be considerably reduced.

41. If the US maintained only a ban on imports from and remittances to China, the potential gains in foreign exchange available to China from a general relaxation of present trade controls would be reduced by roughly one-half.

42. A unilateral US ban affecting only exports to China would not deny any commodities to China which could not be purchased elsewhere, and would have only minor effects in raising China's import costs through preventing the purchase of certain imports in the US market. China would use elsewhere the dollars acquired by exports to the US.

Other Effects on China and the USSR

43. We do not believe that unilateral maintenance of controls by the US would lead to any significant change in Chinese or Soviet courses of action.

Effects on Non-Communist Countries

44. Although trading interests in CHINCOM and Far Eastern countries would welcome the continued absence of US competition in the Chinese market, their governments would be concerned at the divergence of their policies from those of the US. There would probably be apprehension that the failure of the US to participate in the general relaxation of controls would contribute to a continuation of tensions in the Far East. Moreover, difficulties and frictions would probably arise if the US attempted to prevent the re-export to China from third countries of goods imported from the US.

PROBABLE EFFECTS OF RAISING THE LEVEL OF CONTROLS ON TRADE WITH CHINA

45. We have already estimated that controls on exports to China can be only partially effective at a level higher than controls on exports to the European Bloc, because China can procure goods by transshipment via the European Bloc, as long as sufficient shipping or other transport facilities are available. Such transshipment is more costly and time-consuming than direct procurement, but the adverse effect on the over-all Chinese military and economic buildup is relatively small. A further increase in controls on exports to China — without a corresponding increase in the level of COCOM controls — would probably have the effect of increasing the volume of transshipped goods, but it would probably not appreciably retard China's internal development.

46. If an embargo on imports from China, similar to that now applied by the US, were applied by all CHINCOM countries, China would lose export markets now taking about one-quarter of total exports (including Bloc re-exports of Chinese products). Since Bloc markets are not believed to be readily expansible, it is probable that China's import capabilities would be reduced proportionately. Such a reduction in China's imports would significantly retard China's internal development.

[21] Including Foreign Assets Controls.

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47. The increased levels of trade control might give rise to added disagreements and frictions in the relations between China and the remainder of the Bloc, but we do not believe that the basic Sino-Soviet relationship would be seriously disturbed.

48. The Director of Central Intelligence, and the Special Assistant, Intelligence, Department of State, believe that in the unlikely event that *all* non-Bloc shipping and shipping services were denied to the uses of Chinese commerce, the Chinese economy would in the short term be adversely affected and transportation costs increased. Non-Bloc ocean-going vessels in 1953 carried about three-fourths of China's seaborne foreign trade. Bloc flag shipping is inadequate to carry its own trade and no substantial building program is in progress. However, a substantial share of China's seaborne trade now carried in non-Bloc vessels would be carried by the Trans-Siberian railroad and by Bloc flag vessels diverted to the China trade, provided non-Bloc vessels were chartered to replace the shipping so diverted. A considerable part of the trade probably would be curtailed, notably China's exports of coal and iron ore which constitute 40 percent of seaborne export tonnage but less than 1 percent of the value of total exports. These adjustments would probably be made within a reasonable period. If denial affected only CHINCOM flag shipping and services, the Chinese could shift at least part of their seaborne commerce to non-CHINCOM flag vessels, thus mitigating still further the effects described above.

49. The Director of Naval Intelligence; the Deputy Director for Intelligence, The Joint Staff; the Assistant Chief of Staff, G–2; and the Director of Intelligence, USAF, believe that in the unlikely event that *all* non-Bloc shipping and shipping services were denied to the uses of Chinese commerce, the effects upon the Chinese economy would be marked and adverse. Non-Bloc ocean-going vessels in 1953 carried about three-quarters of China's seaborne foreign trade. Since Bloc flag shipping is now inadequate to carry its own trade and no substantial building program is in progress, it is probable that only a small portion of this traffic could be carried through an increase or readjustment in the use of Bloc shipping. Denial of all non-Bloc shipping would result in considerable curtailment of China's foreign trade, because the rail transportation facilities within China and those between China and the European Bloc probably are not adequate to handle the additional tonnages involved. If denial affected only CHINCOM flag shipping and services the Chinese could shift at least part of their seaborne commerce to non-CHINCOM vessels, thus mitigating the effects described above. We believe, however, that the extent of this mitigation would not be significant, since the denial of shipping services (re-insurance, bunkering, repair, etc.) by the largest maritime nations, in addition to other pressures which could be brought to bear, would make most non-CHINCOM countries extremely reluctant to commit their vessels to this trade, despite the probability of premium charter rates being offered by the Bloc. Few non-CHINCOM countries have substantial additional tonnage suitable for the China trade, and with few exceptions, the availability of any vessels would be limited by the extent to which they could be replaced on their regular runs by shipping chartered from CHINCOM countries. Moreover, of all non-CHINCOM countries, only Sweden has a significant amount of shipping which could be so used.

50. Without some new and considerable provocation by China, or possibly by the USSR, we believe that an appreciable increase in the level of controls on trade and shipping with China would almost certainly not be agreed to by non-Communist countries.

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APPENDIX

JAPANESE TRADE WITH COMMUNIST CHINA

1. The Japanese had already developed a substantial trade with mainland China during the 1920's and early 1930's. By 1939, eight years after the seizure of Manchuria, mainland China had become Japan's most important trading area (See Table I, page 23). Manchuria and subsequently much of China became protected Japanese markets. By developing Chinese and particularly Manchurian economic resources the Japanese provided themselves with an outlet for capital goods exports and a market for consumer goods. In addition they obtained a secure source for many of Japan's essential raw material requirements, particularly coal, pig iron, iron ore, salt, soy beans, and oil cake (See Table II, page 24).

2. Until the war years 1941–1945, when Japan was largely cut off from other sources of supply, mainland China was more important to Japan as a market than as a source of imports. Japanese exports to mainland China of textiles, steel, and capital equipment were only partially paid for by purchases of essential raw materials and foodstuffs. This export surplus was balanced primarily by Japanese investment in Manchuria and in other areas of China.

3. Japanese postwar trade with mainland China has been relatively insignificant (See Table III, page 25). Although it had revived somewhat by 1950, Sino-Japanese trade was almost completely stopped by the restrictions following the outbreak of the Korean War. Following the armistice in 1953 it began to revive as controls were slightly relaxed. Unlike the prewar period, recent Japanese trade with mainland China has shown an import surplus.

4. The future level of Sino-Japanese trade will be determined primarily by political factors, and secondarily by economic factors. The principal political factors will be: (a) the extent to which China,[22] in conjunction with the USSR, continues to pursue a policy of Bloc autarky, deliberately minimizing trade with non-Communist areas; (b) the extent to which trade will be used by the Bloc as a weapon of economic and political warfare; and (c) the extent to which the non-Communist countries will maintain controls on trade with China. The principal economic factors are: (a) the availabilities for export of Chinese coal, iron ore, salt, soy beans, rice, and other grains; (b) the availability for export of Japanese capital equipment within the framework of existing controls at competitive prices; and (c) the extent to which the non-Communist world offers increasing trade opportunities to Japan.

5. In attempting to determine the possible magnitude of Sino-Japanese trade expansion within existing controls, the Japanese, assuming Chinese agreement, estimate that this trade could probably be raised to some $70 million each way per year by 1957. The Japanese Ministry of International Trade and Industry has estimated that Japan, at this level of trade, might by 1957, import from China the quantities of certain essential commodities listed below:

Commodity	Quantities Imported in 1953	Estimated Imports for 1957
	(Metric Tons)	
Rice	(none)	100,000
Soy Beans	16,000	100,000
Coal	137,000	800,000
Iron Ore	38,000	500,000
Salt	197,000	300,000

[22] Unless otherwise specified, the terms "China" and "Chinese," are used in lieu of "Communist China" or "Chinese Communists."

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6. We believe that Sino-Japanese trade might reach a figure of $70 million each way per year by 1957. However, Chinese exports to Japan of this magnitude might conflict with increasing domestic requirements and with export commitments to the European Bloc, although these conflicts would not necessarily preclude this level of export if China so desired. In any case, Japanese imports from China at this projected level of trade, although almost 2½ times the value of 1953 imports from mainland China, would be less than 3 percent of the projected total of Japanese imports in 1957.

7. If controls on Chinese trade were lowered to the level now applied against other Bloc countries and if China desired to increase substantially trade with Japan, we believe that by 1957 Sino-Japanese trade could probably be raised to at least $100 million each way. It might even reach $150 million each way, but we believe this would require some diversion of Chinese trade from other export markets.

8. The estimate that the $100 million level could be reached is based primarily upon the Chinese capability to export coal and iron ore in greatly increased quantities — a capability which we believe they can exercise without significantly modifying their present trade commitments to the Bloc or their present domestic program. It is probable that the large iron ore deposits on the island of Hainan could be exploited without great expenditure on the part of the Chinese. The iron ore presently produced from Hainan is probably not included in China's internal steel program, but is earmarked for export. In these circumstances, we believe that China could probably increase its production on Hainan alone sufficiently to provide for the export of about 1.5 million tons of iron ore to Japan, a quantity equal to about one-third of Japan's 1953 total iron ore imports of 4.3 million tons. We believe that China could supply a major portion of the coking coal imported by Japan (3.7 million tons in 1953) with relatively small investment. There is some evidence that China produces pig iron in excess of the needs of its own steel industry and may continue to do so for some time. The extent to which there is or will be an exportable surplus is unknown, but there is a possibility that some export of pig iron to Japan could occur.

9. We believe that if controls on trade with China were removed, Japanese exports of machinery, equipment, rolling stock, and other capital goods to China could be considerably increased. Such exports would be significant in contributing to an alleviation of Japan's trade problem, but barring a far-reaching reorientation of China's foreign trade pattern they would fall short of closing Japan's trade gap in the next few years. Moreover, even if all controls on trade with China were eliminated, we believe it very unlikely that trade relations between mainland China and Japan would regain their prewar significance in percentage terms of Japan's total trade. There has been a fundamental change in the Chinese economic situation since the establishment of the Communist regime. China is now firmly committed to a program of industrialization and of integrating its economy with that of the Bloc. As for Japan, it no longer possesses the political control over Manchuria which permitted it to develop that area as an integral part of its own economy and to make China by far its most important trading partner.[23]

10. Trade with China is important to Japan because in the foreseeable future China is the only major market, other than Southeast Asia, with which Japan can hope to achieve a significant increase in trade. The goods in demand by China, i.e., machinery, transport equipment, and other capital goods, are those which Japan has the capacity to produce. Although we cannot determine whether Japan could compete in specific items, Japan could provide a major share of any total increase in Chinese imports from non-Communist countries. If this trade proceeded satisfactorily, any efforts by the Japanese Government to discourage further expansion would meet with political opposition. China could intensify the political effects of an increase in Sino-

[23] Attention is invited to footnote by the Deputy Director for Intelligence, The Joint Staff, to paragraph 39, text.

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Japanese trade if it were willing to accept Japanese goods even at prices above the world market, or if it made trade offers at a time when Japan was having difficulties exporting to other markets.

11. The extent to which Japan will seek to exploit China as a source of raw materials will depend on the quality and price of these goods as well as Japan's balance of payments position in other currencies, particularly dollars and sterling. If China offered its raw materials at prices lower than world prices and at the same time offered to buy Japanese goods, Japan would probably seek to increase its volume of imports from China. On the other hand, Japan under existing circumstances would probably be somewhat reluctant to become dependent on China as the major source for any one of its essential imports. In any event, we believe that Sino-Japanese trade during the next few years will not in itself cause Japan to significantly alter its present orientation to the West barring a serious depression in the Free World accompanied by a drastic curtailment of Japanese trade opportunities.[24]

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[24] Attention is invited to footnote by the Deputy Director for Intelligence, The Joint Staff, to paragraph 31 text.

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TABLE I

JAPANESE TRADE WITH MAINLAND CHINA AS PERCENT OF TOTAL TRADE *

YEAR	EXPORTS AS % OF TOTAL EXPORTS		IMPORTS AS % OF TOTAL IMPORTS	
	ALL CHINA INCLUDING MANCHURIA AND KWANTUNG	MANCHURIA AND KWANTUNG **	ALL CHINA INCLUDING MANCHURIA AND KWANTUNG	MANCHURIA AND KWANTUNG **
1926	22	..	14	..
1930	19	..	14	..
1936	18	14	11	7
1937	19	15	9	6
1938	30	22	15	11
1939	34	25	16	12
1940	35	22	16	9
1941	38	24	21	10
1942 ***	43	28	42	18
1943 ***	43	26	45	13

* Total trade includes Japanese trade with Korea and Taiwan.
** Trade recorded for Kwantung for the most part originated in or was destined for Manchuria and North China.
*** World War II years.

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TABLE II

RELATIVE IMPORTANCE OF CHINA IN JAPAN'S IMPORTS IN SELECTED COMMODITIES, 1936 AND 1940

Commodity	1936			1940		
	Total Japanese Imports * (1,000 metric tons)	Total Imports * from Mainland China (1,000 metric tons)	Imports from Mainland China as % Total Japanese Commodity Imports	Total Japanese Imports * (1,000 metric tons)	Total Imports * from Mainland China (1,000 metric tons)	Imports from Mainland China as % Total Japanese Commodity Imports
Soy beans & other pulses	917	698	76	607	491	81
Oil-bearing seeds	317	273	86	153	74	48
Rice	1,962	0	0	1,687	54	3
Salt (1939)	1,416	627	42	1,967	820	42
Coal * *	6,360	3,411	54	9,896	4,210	42
Iron ore	4,023	1,252	31	5,129	1,222	24
Pig iron	1,095	271	25	854	431	50
Hides & leather	33	13	39	31	12	39
Iron & steel scrap	1,515	61	4	1,393	77	6
Raw cotton	925	28	3	618	64	10

* Japanese trade with Korea and Taiwan is included in total Japanese imports but excluded from the figures used for mainland China.

** Virtually all of Japan's coking coal came from mainland China.

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TABLE III

JAPANESE POSTWAR TRADE

Year	Total Exports (US $ million)	Japanese Exports to Mainland China including Manchuria	% Total	Total Imports (US $ million)	Japanese Imports from Mainland China including Manchuria	% Total
1950	$ 820	$ 20.	2.4%	$ 974	$40	4.1%
1951	1,355	6.	0.4	2,047	22	1.1
1952	1,273	0.6	neg	2,028	15	0.7
1953	1,275	4.5	0.4	2,410	30	1.2
1954 *	1,570	18.	1.1	2,360	42	1.8

* Estimated totals.

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